

Before the  
FEDERAL COMMUNICATIONS COMMISSION  
Washington, D.C.

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In the Matter of	)	
	)	
Implementation of the Pay Telephone	)	CC Docket No. 96-128
Reclassification and Compensation Provisions	)	
of the Telecommunications Act of 1996	)	
	)	
Oklahoma Independent Telephone	)	
Companies Petition for Declaratory Ruling	)	File No. CCB/CPD No. 99-31

FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF THE SECRETARY

JOINT COMMENTS OF  
AMERICAN PUBLIC COMMUNICATIONS COUNCIL  
AND THE OKLAHOMA PAYPHONE ASSOCIATION

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## SUMMARY

In their petition, the Oklahoma Independent Telephone Companies (“Oklahoma Independents”) seek a Commission ruling that they have the right to establish “cost based” rates for payphone access lines (“PALs”). The American Public Communications Council (“APCC”) and the Oklahoma Payphone Association (“OPA”) agree that PAL rates must be cost based, but have a much different view than the Oklahoma Independents as to what constitutes “cost based.”

The NECA worksheets submitted by the Oklahoma Independents in a proceeding before the Oklahoma Corporation Commission (“OCC”) were grossly deficient for the purpose of supporting proposed increases in PAL rates that ranged from 64 to 440 percent. The OCC was right to reject these proposed huge increases, although it erred by doing so on the grounds that PAL rates need not be cost based.

Under the Commission’s Payphone Orders, PAL rates must be (1) cost based using forward looking economic costs; (2) consistent with the goals of Section 276 of the Telecommunications Act to promote competition in the payphone market and promote widespread deployment of payphones to the benefit of the general public; (3) nondiscriminatory and (4) consistent with the Computer III guidelines (*e.g.*, satisfy the “new services test”).

The Oklahoma Independents’ proposed PAL rates fail this test on all counts. The NECA worksheets relied on by the Oklahoma Independents as cost support are not forward looking, do not comply with the new services test, and are designed for a purpose — the calculation of Universal Service Fund settlements — that is entirely different from

that of providing cost support for rates. Moreover, reliance on the NECA worksheets would not reflect the resulting double recovery in costs. As facilities-based carriers, the Oklahoma Independents receive revenues from a number of sources – *e.g.*, the SLC, PICC, state and federal universal service funds and access charges – that are designated for recovery of local loop costs. For the PAL rate to be “cost-based,” it must be set at a level that represents that portion of the total cost of the line that is not being recovered through other sources.

Reliance on the NECA worksheets to justify PAL rates also would frustrate the goals of Section 276 and would be discriminatory. Competitive providers, faced with exorbitant charges, may decline to install payphones in locations they otherwise would serve if PAL rates were reasonable. LEC payphone providers, because they would incur a cost significantly below what competitive providers must pay, could serve such locations.

Even if the Commission were to decline to impose the full-blown requirements of its Payphone Orders on the small-LEC Oklahoma Independents, it must fashion its guidance to the OCC to establish PAL rates for the Oklahoma Independents in a way that is consistent with the spirit and intent of the Payphone Orders and the mandates of Section 276.

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<b>Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996</b>	)	<b>CC Docket No. 96-128</b>
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<b>Oklahoma Independent Telephone Companies Petition for Declaratory Ruling</b>	)	<b>File No. CCB/CPD No. 99-31</b>

**JOINT COMMENTS OF  
AMERICAN PUBLIC COMMUNICATIONS COUNCIL  
AND THE OKLAHOMA PAYPHONE ASSOCIATION**

The American Public Communications Council ("APCC") and the Oklahoma Payphone Association, pursuant to the Commission's Public Notice DA 99-2061 released October 4, 1999, hereby submit their initial joint comments on the above-referenced Petition for Declaratory Ruling ("Petition") of the Oklahoma Independent Telephone Companies ("Oklahoma Independents" or "Petitioners").

**I. INTRODUCTION.**

**A. The Petition.**

In their Petition, the Oklahoma Independents seek a Commission ruling that they have the right to establish "cost-based" rates for payphone access lines ("PALs"). Petition, p. 8. The Oklahoma Independents purportedly had attempted to file "cost based" PAL rates, but their efforts were disallowed by an April 16, 1999 order of the Oklahoma Corporation Commission ("OCC") (the "OCC Order"). Petition, p. 2. The Oklahoma Independents ask the Commission to declare that the OCC Order is contrary to

the Commission's pricing guidelines and "to direct the OCC to undertake further proceedings consistent with the Commission's directives." Petition, p. 3.

In other jurisdictions, establishing cost based PAL rates has resulted in significant reductions in the charges paid by payphone providers.<sup>1</sup> By contrast, as shown in the following table, the application of purportedly "cost-based" PAL rates proposed by the Oklahoma Independents would greatly increase the charges paid by payphone providers:

Oklahoma Independents	Current Rate	Proposed Rate	Percentage Increase
Eaglenet, Inc.	\$31.30	\$51.30	64%
Valliant Tel. Co.	19.40	45.89	137%
KanOkla Telephone Association, Inc.	12.45	66.50	434%
Santa Rosa Telephone Cooperative	13.00	70.22	440%
Oklahoma Telephone & Telegraph	15.35	81.73	432%
Chickasaw Telephone Company	25.50	61.27	140%
Pine Telephone Company	23.25	64.64	178%

As APCC/OPA show below, the costing methodology used by the Petitioners in the OCC proceeding resulted not only in inflated costs but double recovery of those costs. While APCC/OPA agree with Petitioners that PAL rates must be cost based, such cost-based rates, if properly developed, are unlikely to yield PAL charges significantly higher than their current levels.

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<sup>1</sup> See, e.g., South Carolina Public Service Commission's April 19, 1999 Order Setting Rates for Payphone Lines and Associated Features (Order No. 1999-285) and July 19, 1999 Order on Requests for Reconsideration and Clarification in Docket No. 97-124-C (Order No. 1999-497) (reducing proposed PAL rate from \$45.75 to \$25.49); and Delaware Public Service Commission's November 4, 1997 Findings, Opinion & Order No. 4637 in Docket No. 97-103T (reducing proposed flat rate component of PAL rates from \$22.68 to \$16.63).

## **B. Statement of Interest.**

APCC is a national trade association representing over 2,000 primarily independent (non-local exchange carrier), competitive providers of pay telephone equipment, services and facilities. APCC members offer payphone services throughout the country, including rural areas such as those in which the Oklahoma Independents serve as the incumbent local exchange carrier ("ILEC"). APCC seeks to promote competitive markets and high standards of service for pay telephones. To this end, APCC actively participates in Commission proceedings affecting payphones.

OPA is a state trade association representing over thirty competitive payphone service providers certificated by the OCC to provide payphone services in Oklahoma. OPA's members provide payphone services throughout the State of Oklahoma, including the rural areas in which the Oklahoma Independents serve as the ILEC. OPA was a party in the proceedings before the OCC that resulted in the OCC Order at issue.

## **II. THE OKLAHOMA INDEPENDENTS ARE CORRECT THAT PAL RATES MUST BE COST BASED.**

The Oklahoma Independents correctly assert in the Petition that the OCC Order contravenes the directive in the Commission's Payphone Orders<sup>2</sup> that PAL rates be

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<sup>2</sup> Report and Order, 11 FCC Rcd 20541 (1996) (*Report and Order*); Order on Reconsideration, 11 FCC Rcd 21233 (1996) (*Reconsideration Order*) (together the *Report and Order* and the *Reconsideration Order* are referred to as the *Payphone Orders*). The *Payphone Orders* were affirmed in part and vacated in part. See *Illinois Public Telecomm. Ass'n v. FCC*, 117 F.3d 555 (D.C. Cir. 1997) ("*Illinois Public Telecomm.*"). The Commission addressed the issues remanded by *Illinois Public Telecomm.* in the Second Report and Order, 13 FCC Rcd 1778 (1997) (*Second Report and Order*). The *Second Report and Order* was also appealed. On appeal, the Court remanded certain issues to the Commission. See *MCI Telecomm. Corp. et al. v. FCC*, 143 F.3d 606 (D.C. Cir. 1998) (footnote continued on next page)

cost-based. Petition, pp. 4-7. However, Petitioners do not address in any detail the flawed reasoning underlying the OCC Order. APCC provides the following analysis of the OCC Order.

**A. The OCC Order Distinguished Between Central Office Coin Service Lines And Pals, And Wrongly Concluded That The Commission's Payphone Orders' Directive Re Cost-Based Rates Applies Only To Coin Lines.**

In its Order, the OCC distinguishes between PALs and central office coin service lines ("Coin Lines"). OCC Order, p. 2.<sup>3</sup> This conclusion in the OCC Order was based on the November 28, 1998 Report of the Administrative Law Judge ("ALJ Report"). The ALJ Report states (at pp.2-3):

The [Oklahoma] Commission Staff's position was that the FCC did not intend for the payphone access line to be cost based and unsubsidized, only the central office coin features associated with payphone access lines. The result of developing cost based, unsubsidized rates for the Applicants would be a higher rate than their business access line rate. The OPA stated that the payphone access line rates developed by the Applicant's [*sic*] were higher than their business access line rate, and rather than being unsubsidized and cost based, should be in accordance with the LECs overall revenue picture, including all subsidies and revenue sources.

The ALJ adopted the Staff's position and ruled that:

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(*MCI v. FCC*). The Commission addressed the issues on remand in The Third Report and Order, CC 99-7, rel. February 4, 1999.

<sup>3</sup> PALs are "dumb" lines used with "smart" payphones (*i.e.*, payphones with internal computers that perform many of the functions associated with setting up, completing, and billing for a payphone call). Central office coin transmission service lines ("Coin Lines") are "smart" lines used with "dumb" phones (*i.e.*, payphones that rely on equipment located at the LEC's central office to perform many of the functions that are performed by a "smart" payphone). The vast majority of payphones operated by competitive payphone providers are "smart" payphones with "dumb" lines (*i.e.*, PALs). The vast majority of payphones operated by ILECs are "dumb" payphones that use "smart" lines (*i.e.*, Coin Lines).



. . . the FCC never intended for the LECs to provide cost support for payphone access lines or prove their access lines are cost based. Rather, the FCC's Payphone Orders require the unbundled central office coin services to be supported with cost data. The payphone access lines must be priced in accordance with the LECs [*sic*] overall cost revenue picture.

ALJ Report, p. 3.

The OCC Staff's position referred to in the ALJ Report was based on the Staff's reading of paragraph 146 of the Commission's Report and Order and paragraph 163 of the Reconsideration Order. See Staff's Brief filed October 29, 1998 (copy attached as Appendix A), pp. 2-3. While paragraph 146 of the Report and Order does appear to address only the requirement for cost-based rates for Coin Lines, the OCC Staff's argument collapses when it gets to paragraph 163 of the Reconsideration Order. The OCC Staff stated as follows in its Brief (p. 4):

This interpretation [that PAL rates need not be cost-based] is further supported by the FCC in its Reconsideration Order at paragraph 163, where the FCC draws a clear distinction between "LEC payphone services" and the actual payphone "lines" by stating, "LECs are not required to file tariffs for the basic payphone lines for smart and dumb payphones . . . ." Such a statement would not make sense unless the FCC clearly intended to draw such a distinction between the unbundled "services" and the "lines."

The OCC Staff quotes paragraph 163 of the Reconsideration Order out of context.

The context of the quote is as follows:

LECs are not required to file tariffs for the basic payphone line for smart and dumb payphones with the Commission. We will rely on the states to ensure that the basic payphone line is tariffed by the LECs in accordance with the requirements of Section 276. [Emphasis supplied.]

The Commission is not distinguishing between "lines" and "services" here. The Commission is merely reiterating its announcement in paragraph 162 of the

Reconsideration Order of its decision to “modify the federally [*sic*] tariffing requirement” of its Report and Order by having LECs file their payphone line (Coin Line and PAL) tariffs with state commissions rather than with the Commission. Indeed, the Commission makes its intention crystal clear in paragraph 163 that by “basic payphone line,” it means that lines/services for both “smart and dumb payphones” (*i.e.*, for PALs as well as Coin Lines) must be tariffed in accordance with the cost-based and other requirements of Section 276.

The OCC Staff also reasoned (Brief, p. 4) that:

This position [that PAL rates need not be cost-based] is even further supported when one considers the impact of allowing a LEC, in a filing such as these, to implement a “cost-based” access line rate for a single “class” of customers – PSPs. It is difficult to imagine that the FCC would condone “piece-meal” ratemaking for a rate-of-return regulated entity. Nor, would it be logical for the FCC or this Commission to suggest “rate rebalancing” solely for payphone access lines, at the expense of the other classes of subscribers who receive the same type of access to the same type of line.

What the OCC Staff overlooks is that the Commission’s policy of requiring PAL rates to be cost based, even if LEC rates for other services are not, stems from the fact that the mandate of Section 276 addresses payphone services only, not other LEC services. Moreover, while the OCC’s concern for the potential impact of requiring a LEC that receives universal service support to file cost-based rates is a legitimate concern, it cannot justify excising LECs wholesale from the cost-based requirements of Section 276. Rather, the OCC’s concern about line rates that receive universal service should be addressed, as APCC/OPA show below, by correct implementation of the requirement to avoid over-recovery of costs.

**B. The Commission's Reconsideration Order, And The Commission's Common Carrier Bureau April 4, 1997 And April 15, 1997 Waiver Orders Make Clear That Pals As Well As Coin Lines Must Be Cost Based.**

The Commission makes clear in its Reconsideration Order that PALS are included in the "basic payphone services:"

Accordingly, as required in the Report and Order, LECs must provide tariffed, nondiscriminatory basic payphone services that enable independent providers to offer payphone services using either instrument-implemented "smart payphones" or "dumb" payphones that utilize central office coin services, or some combination of the two in a manner similar to the LECs. LECs must file those tariffs with the state.

Reconsideration Order, ¶162.

The Commission also makes clear in the Reconsideration Order that PALS, like other basic payphone services, must be cost based:

We require LECs to file tariffs for the basic payphone services and unbundled functionalities in the intrastate and interstate jurisdictions as discussed below. LECs must file intrastate tariffs for these payphone services and any unbundled features they provide to their own payphone services. The tariffs for these LEC payphone services must be: (1) cost based; (2) consistent with the requirements of Section 276 with regard, for example, to the removal of subsidies from exchange and exchange access services; and (3) nondiscriminatory. States must apply these requirements and the Computer III guidelines for tariffing such intrastate services.

Reconsideration Order, ¶ 163.

The Common Carrier Bureau's April 4, 1997 Waiver Order echoes the Reconsideration Order's directives:

In the Order on Reconsideration, the Commission required LECs to file tariffs for the basic payphone services and unbundled functionalities in the intrastate and interstate jurisdictions. *Basic payphone services for instrument-implemented "smart" payphones, "dumb" payphones, and inmate payphones, including any features and functions that the LEC has unbundled from the basic payphone*

line, which enable independent providers to offer payphone services, and unbundled features and functions provided by a LEC to its payphone operations, *must be tariffed at the state level*.

....

The plain language of the Order on Reconsideration provides that *state tariffs for payphone services must be cost based*, consistent with the requirements of Section 276, nondiscriminatory, and consistent with Computer III guidelines.

April 4, 1997 Waiver Order, ¶¶ 8, 31 (emphasis supplied).

The Common Carrier Bureau's April 15, 1997 Waiver Order further supports the view that PALs as well as Coin Lines must be cost-based:

The Commission concluded in the Order on Reconsideration that LECs are required to tariff basic payphone lines (smart, dumb, and inmate) at the state level only.

....

The requirements for intrastate tariffs are: (1) that payphone service intrastate tariffs be cost-based, consistent with Section 276, nondiscriminatory and consistent with Computer III tariffing guidelines; and (2) that the states ensure that payphone costs for unregulated equipment and subsidies be removed from the intrastate local exchange service and exchange access service rates.

April 15, 1997 Waiver Order, ¶¶ 9, 10.

**C. It Would Flatly Contradict The Pro-Competitive Purpose Of Section 276 And The Payphone Orders To Require Cost Based Rates For Coin Lines But Not For PALs.**

One of the fundamental purposes of Section 276 and the Payphone Orders is to promote competition among payphone providers. Virtually all competitive payphone providers lease “dumb” PALs, not “smart” Coin Lines, for use with their “smart” payphones. Therefore, it would make no sense for the Commission to require cost-based rates for Coin Lines but not for PALs. ILECs that provide payphone services primarily

through “dumb” payphones connected to “smart Coin Lines have every incentive to set high rates for the PALs that their competitor payphone providers must use to connect their “smart” payphones.

Because the ILECs still are essentially monopoly providers of PALs, competitive payphone providers have two choices if an ILEC is able to establish high rates for PALs: exit the market or purchase PALs from the ILEC at the price the ILEC has set. Such a result would flatly contradict Section 276’s goals of promoting competition among payphone providers and promoting the widespread deployment of payphone services to the general public, and must not be allowed.

### **III. PAL RATES MUST MEET THE REQUIREMENTS OF THE COMMISSION'S PAYPHONE ORDERS.**

The Oklahoma Independents quote with approval from the Commission’s Reconsideration Order that PAL rates must be (1) cost based, (2) consistent with the requirements of Section 276, (3) nondiscriminatory and (4) consistent with Computer III guidelines. Petition, p. 7. APCC/OPA agree that these four elements form the applicable standard the Oklahoma Independents must meet when establishing PAL rates (or Coin Line rates for that matter). However, as discussed below, APCC/OPA’s view as to what constitutes compliance with the standard varies widely from that of the Oklahoma Independents, and highlights the need for the Commission to issue clear guidance as to what it means by “cost-based.”

The Commission is being asked to make determinations regarding how the elements of its four-part standard are to be applied to small, rate of return regulated LECs.

The application of the Commission's standard should be performed in a way that meets two fundamental criteria:

(1) Each element of the four part standard must be applied in a way that does not render another element (or elements) of the test meaningless; and

(2) The elements of the four-part standard, applied as a whole, must allow the objectives of Section 276 to be met.

When applied in this manner, the Commission's four-part standard will permit certain of the concerns stated by the OCC's Staff to be addressed without excluding PAL rates from the Commission's requirements.

**A. The Oklahoma Independents' Cost Data Is Wholly Inadequate.**

The limited cost data supplied by the Petitioners is insufficient to use as a basis for cost based rates. Petitioners have supplied only NECA worksheets for the Calculation of Projected Universal Service Fund. The methodology underlying these worksheets is designed to determine, through a series of allocations, the amount of any needed USF settlements. The worksheets *are not, and do not purport to be*, a cost study of the elements of a PAL (or of any other elements of payphone access service). The NECA worksheets represent an inherently arbitrary allocation process designed to accomplish a fundamentally different objective than that of justifying rates. There is simply no basis to interpret any of the values generated by the worksheet as a measure of the Oklahoma Independents' "cost" of providing any network functionality, including PALs. Even if the Commission were to determine that small, rate of return regulated LECs should establish cost based rates for

PALs based on some measure of embedded costs, a “Study Area USF Cost per Loop,” as produced by the NECA worksheets, is not a substitute for the results of study of the cost of local loops.

The Petitioners’ reported costs for local usage (switching) also make the NECA cost data, and the method used to develop it, suspect. Local usage is also a component of payphone access service, and it is necessary for the LECs to conduct a properly performed study of these costs as well. In a table submitted to the OCC (attached as Appendix B), Petitioners indicate that their calculation of switching costs per month ranges from \$19.62 to \$32.56. At three minutes per call and 200 calls per month (typical values for a rural payphone), Petitioner’s information yields a per MOU cost of 3.2 to 5.3 cents. This cost per MOU is 10 to 20 times the cost reported by other LECs, even for the smallest central offices. As a result, Petitioners’ cost results, and the methodology used to create them, must be considered suspect.

In reviewing the Oklahoma Independents’ proposed rates, the OCC Staff stated (Brief, p. 4):

Despite the parties’ previous suggestions to the contrary, it is inconsistent with the Payphone Reclassification Orders, and *it would be irresponsible of Staff to condone the applicant’s or this Commissions [sic] reliance on the cost support documentation the applicants have provided thusfar, in support of increasing payphone access line rates.* Such was not the intent of the FCC and it is certainly not in the public’s interest. [Emphasis supplied.]

APCC/OPA concur fully with the OCC Staff’s view.

**B. Petitioners' PAL Rates Can And Should Be Developed Using Forward-Looking, Economic Costs.**

The Oklahoma Independents suggest that because they are rate of return rather than price-cap carriers, they use the alternative cost support methodologies in Section 61.39 of the Commission's Rules. Petition, footnote 15. However, as other LECs have amply demonstrated, the operation of the Oklahoma Independents pursuant to rate of return regulation does not preclude them from conducting PAL cost studies consistent with a forward looking economic cost methodology.<sup>4</sup>

The operation of a LEC pursuant to rate of return regulation does not mean that it does not incur economic, rather than regulatory, costs. It only means that its rates are not typically set utilizing this method. Once forward looking economic cost data are developed, "cost based" rates for payphone access lines can be developed by considering the total economic (*e.g.*, Total Service Long Run Incremental Cost, or "TSLRIC"<sup>5</sup>) costs and the sources of revenue received for the recovery of those costs.

This same information would allow Petitioners to demonstrate compliance with the new services test as required by fourth element of the Commission's four-part standard

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<sup>4</sup> To the extent that the Petitioners do not currently have the capability to conduct TSLRIC studies, universal service models currently under development will make that capability widely available in the foreseeable future.

<sup>5</sup> APCC/OPA agree with a previous conclusion of the Commission that TSLRIC represents an appropriate and practical measure of forward looking economic costs: "[P]rices . . . should be set at forward-looking long-run economic cost. In practice, this will mean that prices are based on TSLRIC. . . ." Implementation of Local Competition Provisions in the Telecommunication Act of 1996, First Report and Order, 11 FCC Rcd 15499, 15844 (¶ 672) (1996).



(consistency with Computer III guidelines). The NST originally was used by the Commission in an effort to set the proper rates for Basic Service Elements in the context of the FCC's Open Network Architecture ("ONA") initiatives in CC Docket No. 89-79. The pricing methodology was adopted by the Commission as a condition to local exchange carriers offering enhanced retail services in competition with competitive enhanced service providers ("ESPs") in the Computer III proceedings. In its initial ONA Notice of Proposed Rulemaking, the Commission sought comment on a pricing mechanism to allow ILECs into the enhanced services industry, knowing full well that ILECs had the opportunity to charge their competitors in the enhanced services industry unreasonably high prices for those necessary inputs to the service.

By identifying incremental costs, the SCIS model would provide a floor that ensures that existing access services, such as basic switching, are not subsidizing new, unbundled BSEs or qualified non-ONA services. However, the model produces only a cost suitable for determining the level below which BSEs should not be priced. It does not yield a cost suitable for establishing a maximum rate. We seek comment on whether such a ceiling would be necessary in light of the overall constraint on switched element revenues, and if so, how such a ceiling could be developed.

*In the Matter of Amendments of Part 69 of the Commission's Rules Relating to the Creation of Access Charge Supplements for Open Network Architecture*, Notice of Proposed Rulemaking, 4 FCC Rcd 3983, ¶ 20 (1989).

The Commission, in adopting the new services test, as the method to determine the price ceiling as well as the price floor, stated:

Although the price cap system has rules designed to ensure that the adjustments of existing prices will be reasonable, prior to the adoption of the interim new services test, it did not provide any specific tariff review showing to ensure that initial prices for "new" services were

not unreasonably high. A net revenue test provides assurance that the initial price will not be set at a predatory level [*i.e. a price floor*], but does not ensure that the initial rate will not be excessive. . . . As NYNEX recognizes, a cost-based upper bound can preserve carriers' incentives to innovate, if it permits them to earn a return on their total new investment commensurate with the risk they assume.

*Open Network Architecture*, Report and Order & Order on Further Reconsideration and Supplemental Notice of Proposed Rulemaking, 6 FCC Rcd 4524, ¶¶ 38-42 (1991) (comment added). Consistent with the new services test, a properly performed economic cost study would allow a small, rate of return regulated LEC to demonstrate that the level of direct cost and the amount of the overhead loading added to that direct cost are reasonable.

There are two ways by which PAL rates based on economic costs would support the stated objectives of Section 276 to “promote competition among payphone service providers and promote the widespread deployment of payphone services to the benefit of the general public,” and the objectives of the Commission’s Payphone Order. First, rates set in this manner will be economically efficient, which will result in prices to the end users of payphone services that reflect the value of the resources consumed to the benefit of the public at large.

Second, competitive payphone service providers and ILECs will be able to compete on an equal footing. Both will incur a cost of doing business for the PAL functionality that is equal to the forward-looking, economic cost. As a result, a key component of the “nondiscriminatory” requirement will be met, and the ability of the LECs to engage in anticompetitive practices in favor of their own payphone operations will be diminished.

In direct contrast, PAL rates based on the “cost data” proposed by the Petitioners would have direct adverse consequences for both competitive payphone providers and the Commission’s efforts to meet the objectives of Section 276. PAL rates, if established at the exorbitant levels proposed by Petitioners, would seriously impair competition in the payphone market and the widespread deployment of payphones. If PAL rates are set at these inflated levels, competitive payphone providers will incur a cost of doing business for the PAL functionality that is equal to the inflated rate, while the LEC will incur a potentially significant lower cost equal to the economic cost of providing the PAL.

In addition, a competitive provider’s decision to place a phone at a given location depends, as it must, on the expected revenues from that phone and the cost of placing and operating the unit. If PAL rates are set at excessive levels, competitive providers will be unable to make a business case for placing phones at certain geographic locations, even though a business case for placing the phone could have been made if the PAL line rate had been set based on its economic cost. Because petitioners are now seeking to increase rates by 64 to 440 percent, competitive providers are likely to find that phones that have been previously placed in certain locations can no longer be justified at the proposed rates for payphone access service, and will be forced into a business decision to remove those phones.

If that happens, the location may be served by the incumbent LEC (who can make a business case to do so because it will incur a cost of doing so that is significantly less than the rate being charged to PSPs, in direct violation of the Commission’s

nondiscriminatory requirement) or the location may go unserved to the detriment of the public. Excessive PAL rates represent a clear roadblock to Section 276's objective to promote competition and the widespread deployment of payphones.

**C. "Cost Based" Rates For Payphone Access Lines Must Be Established At A Level That Will Avoid Double Recovery Of The LEC's Costs.**

Another flaw in the "cost data" relied on by Petitioners is that it would allow double recovery of costs. As facilities-based carriers, Petitioners receive revenues from a number of sources that are designated for recovery of the non-traffic sensitive ("NTS") components of the network (generally, the local loop and the switch line port). For lines provided as PALs, these revenue sources include the Subscriber Line Charge ("SLC") or End User Common Line Charge ("EUCL"),<sup>6</sup> the Presubscribed Interexchange Carrier Charge ("PICC"),<sup>7</sup> disbursements from federal and state universal service funds, interstate and intrastate access rate elements designed for NTS recovery, and finally the PAL rate.

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<sup>6</sup> The Commission has characterized the SLC as follows:

Incumbent LECs assess end users a flat end user common line charge (EUCL), also known as the subscriber line charge (SLC), to recoup part or all of the local loop costs allocated to the interstate jurisdiction.

In the Matter of Access Reform, *et al.*, CC Docket No. 96-262, Notice of Proposed Rulemaking, 11 FCC Rcd 21354, ¶ 27 (1996).

<sup>7</sup> The Commission characterized the purpose of the PICC and the SLC as the same:

The PICC is not a universal service mechanism, but rather a flat-rated charge that recovers local loop costs in a cost-causative manner.

*Id.*, at ¶104.

For the PAL rate to be “cost based,” it must be set at a level that represents the portion of the total costs of the line (whether calculated on an economic or embedded basis) that are not being recovered through other charges designated for that purpose.

A TSLRIC study of the cost of a PAL includes total, non jurisdictionally separated costs. Similarly, a properly performed embedded cost study will include total unseparated costs. As a result, it is necessary to consider both interstate and intrastate sources of revenue when establishing a cost based rate for PALs (*i.e.*, determining that portion of the total cost of the access line that is not being recovered through another interstate or intrastate charge).

Petitioners seek the establishment of a PAL rate that would allow them to double-recover at least a portion of their costs. Specifically, they argue for a rate that would fully recover the total “cost”<sup>8</sup> that they have identified while ignoring the other sources of revenue that they currently receive (*e.g.*, from SLCs, PICCs, universal service funds, access charges). Such a pricing scheme would allow a LEC operating pursuant to either price caps or rate of return regulation to double recover the costs associated with a PAL.

For rate of return regulated LECs, an additional problem is created. The establishment of a PAL rate that recovers the total identified cost while ignoring other sources of revenue designated for the recovery of a portion of those costs will necessarily require a downward adjustment to, or elimination of, those other sources of revenue. As

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<sup>8</sup> As described above, Petitioners have not provided a cost study of PALs per se, but instead have offered the results of a NECA worksheet for the calculation of USF settlements.

the OCC Staff correctly pointed out (Brief, p. 4), such an interpretation of the “cost based” element of the Commission’s four-part standard would require that the Petitioner’s rates be “rebalanced” as a part of a larger process, a result that would not be “logical.”

The OCC Staff’s observations illustrate the fallacy in the Petitioner’s proposal to establish “cost based” rates in the absence of a cost study. Petitioners are proposing to increase PAL rates to an arbitrarily higher level that is based on the results of a NECA USF settlements worksheet. Such an increase will allow for the double recovery of costs unless, as OCC Staff correctly points out, such a rate increase is made in conjunction with adjustments to other of the Petitioners’ rates pursuant to their operation under rate of return regulation.

The “zero sum game” of rate of return regulation means that Petitioners’ methodology would allow them to justify a PAL rate as “cost based” that ranges from a low of the economic cost of providing the lines to a high of the LEC’s total revenue requirement. Even if one accepts the absurd notion that such a process can be relied upon to yield rates that are “cost based,” such a mechanism cannot be reliably used to develop rates that are nondiscriminatory and that will “promote competition among payphone providers and promote the widespread deployment of payphone services to the benefit of the general public.”

**D. In The Absence Of A Cost Study, Proxy Rates Should Be Developed Consistent With The Objectives Of Section 276.**

In order to establish PAL rates that comply with Commission's Payphone Orders, the LEC must produce, and the state regulator must approve, properly performed cost studies. In order for these rates to be economically efficient, promote competition and promote the widespread deployment of payphones, these studies must determine the forward-looking economic (TSLRIC) cost of the PAL and any overhead costs that are to be included in the rate.

Absent such studies, meaningful application of the "cost based" requirement or the new services test cannot be accomplished. If a LEC demonstrates to the Commission that it is unable to perform the necessary cost study, the Commission should direct the state regulator to develop cost based rates for payphone access services utilizing the cost proxy model that it has adopted for use in calculating universal service fund requirements. In the absence of a LEC-provided cost study, this cost proxy information – in conjunction with the cost offsets identified previously<sup>9</sup> – can be used to establish a reasonable proxy for a cost based rate. The Commission should not permit the LECs to establish rates at arbitrarily high levels under the guise of setting a "cost based" rate in a way that renders the remaining elements of the four-part test meaningless, as the Petitioners seek to do here.

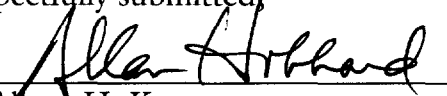
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<sup>9</sup> As described in section 4C, recognition of these cost offsets is necessary to avoid a double recovery by the LEC of certain costs.

#### IV. CONCLUSION.

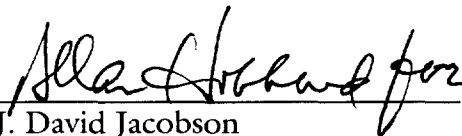
The Payphone Orders require all LECs to offer cost-based rates for PALs as well as Coin Lines. Because of the potential impact of huge rate increases on competitive payphone providers and the consuming public in rural areas, the Commission must fashion its guidance to the OCC in a way that is consistent with the goal of Section 276 to promote competition in the payphone market and the widespread deployment of payphones, but without construing its Payphone Orders in a way that erodes the requirement that mid-sized and large LECs establish properly cost-based payphone line rates.

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**APPENDIX A**  
**TO**  
**JOINT COMMENTS OF**  
**AMERICAN PUBLIC COMMUNICATIONS COUNCIL**  
**AND**  
**OKLAHOMA PAYPHONE ASSOCIATION**  
**(in CC Docket No. 96-128 and File No. CCB/CPD No. 99-31)**

**FILED**

OCT 29 1998

BEFORE THE CORPORATION COMMISSION OF THE STATE OF OKLAHOMA  
CORPORATION COMMISSION  
OF OKLAHOMA

IN THE MATTER OF THE APPLICATION OF EAGLENET, INC. FOR APPROVAL OF TARIFFS	) ) )	CAUSE NO. PUD 970000024
IN THE MATTER OF THE APPLICATION OF VALLIANT TELEPHONE COMPANY FOR APPROVAL OF TARIFFS	) ) )	CAUSE NO. PUD 970000025
IN THE MATTER OF THE APPLICATION OF KANOKLA TELEPHONE ASSOCIATION INC. FOR APPROVAL OF TARIFFS	) ) )	CAUSE NO. PUD 970000027
IN THE MATTER OF THE APPLICATION OF SANTA ROSA TELEPHONE COOPERATIVE, INC. FOR APPROVAL OF TARIFFS	) ) )	CAUSE NO. PUD 970000082
IN THE MATTER OF THE APPLICATION OF OKLAHOMA TELEPHONE & TELEGRAPH, INC. FOR APPROVAL OF TARIFFS	) ) )	CAUSE NO. PUD 970000141
IN THE MATTER OF THE APPLICATION OF CHICKASAW TELEPHONE COMPANY FOR APPROVAL OF TARIFFS	) ) )	CAUSE NO. PUD 970000187
IN THE MATTER OF THE APPLICATION OF PINE TELEPHONE COMPANY FOR APPROVAL OF TARIFFS	) ) )	CAUSE NO. PUD 970000188
IN THE MATTER OF THE APPLICATION OF ALLTEL OKLAHOMA, INC. FOR APPROVAL OF REVISIONS TO ITS LOCAL EXCHANGE TARIFFS	) ) ) )	CAUSE NO. PUD 970000015
IN THE MATTER OF THE APPLICATION OF OKLAHOMA ALLTEL, INC. FOR APPROVAL OF REVISIONS TO ITS LOCAL EXCHANGE TARIFFS	) ) ) )	CAUSE NO. PUD 970000016
APPLICATION OF OKLAHOMA COMMUNICATION SYSTEMS, INC. FOR APPROVAL OF REVISIONS TO ITS GENERAL EXCHANGE TARIFF.	) ) ) )	CAUSE NO. PUD 970000118
IN THE MATTER OF THE APPLICATION OF MID-AMERICA TELEPHONE COMPANY, INC., FOR APPROVAL OF REVISIONS TO ITS GENERAL EXCHANGE TARIFF.	) ) ) ) )	CAUSE NO. PUD 970000119
IN THE MATTER OF THE APPLICATION OF WYANDOTTE TELEPHONE COMPANY FOR APPROVAL OF REVISIONS TO ITS GENERAL EXCHANGE TARIFF.	) ) ) ) )	CAUSE NO. PUD 970000120

STAFF'S SECOND BRIEF

COMES NOW Ernest G. Johnson, Director, Public Utility Division, Oklahoma Corporation Commission, on behalf of the Commission Staff ("Staff"), and pursuant to the directives of the Administrative Law Judge, respectfully submits the following brief concerning the interpretation of pertinent provisions of §276 of the Federal Telecommunications Act of 1996 ("Act")<sup>1</sup>, and Federal Communication Commission ("FCC") orders issued in CC Docket Nos. 96-128 and 91-35<sup>2</sup>

<sup>1</sup>Much time and energy has been expended by the parties to these Causes. Regrettably, with the passage of time, the issues have become somewhat blurred and confusing. Questions have arisen with regard to the cost support documentation submitted, the applicability of that cost support documentation to the access line rates of the applicants, and even what the statute and the FCC actually require in that regard.<sup>4</sup>

This brief is intended to bring clarity to these cases, not necessarily by attempting to address the myriad of undefined issues that appear to exist today, but by identifying the pertinent provisions of the statute and the Payphone Reclassification Orders and identifying the NON-issues.

#### Applicable law governing the causes.

§276(b)(1) of the Act directs the FCC to prescribe regulations that:

"(B) discontinue the intrastate and interstate carrier access charge payphone service elements and payments in effect on such date of enactment, and all intrastate and interstate payphone subsidies from basic exchange and exchange access revenues, in favor of a compensation plan as specified in subparagraph (A) . . ."

In fulfillment of its obligation under §276 of the Act, the FCC initiated a rulemaking<sup>3</sup> which resulted in the issuance of the Payphone Reclassification Orders<sup>4</sup>. In these orders, the FCC specifically discusses and adopts rules for each of the categories it was directed to address in §276(b). A brief review of the "Table of Contents" of the Payphone Reclassification Orders, attached hereto at Tab "1", and its comparison with §276(b), attached hereto at Tab "2", reflects how the pertinent provisions of the two documents correspond to each other (i.e.: issue "A" in the Payphone Reclassification Orders addresses "Per-call Compensation" issues as the FCC was directed to do in §276(b)(1)(A), and issue "B" titled, "Reclassification of LEC-owned Payphones" corresponds directly to §276(b)(1)(B) of the Act, and specifically addresses those issues).

#### Issues v. Non-issues.

The specific question that is purportedly at issue, for purposes of this brief, is:

**"Whether the FCC's Payphone Reclassification Orders require that an Incumbent Local Exchange Carrier's ("ILEC's") payphone access line rate be based upon unsubsidized cost based rates?"**

Based upon Staff's extensive review of the Payphone Reclassification Orders, the simple answer is, "NO". This answer can be supported by a review of the following provisions<sup>5</sup> of the Payphone Reclassification Orders:

<sup>1</sup> 47 U.S.C. §276(b)(1)(B).

<sup>2</sup> Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996, CC Docket No. 96-128, Notice of Proposed Rulemaking, 11 FCC Rcd 6716 (1996), Report and Order, FCC 96-388, released September 20, 1996 ("Payphone Order"). Order on Reconsideration, FCC 96-439, released November 8, 1996 ("Reconsideration Order"), aff'd in part, rev'd in part, Illinois Public Telecommunications Association v. FCC, Case No. 96-1394 (D.C. Cir., July 1, 1997) (hereafter referred to collectively as "Payphone Reclassification Orders").

<sup>3</sup> Id.

<sup>4</sup> Id.

<sup>5</sup> Paragraphs 127 through 191 of the Payphone Order, and paragraphs 142 through 208 of the Reconsideration Order.

At paragraph 128 of its Payphone Order, the FCC restates §276(b)(1)(B) of the Act. As it then goes on to explain, the rationale behind the statutory requirement is that, "Currently, incumbent LEC payphones, classified as part of the [LEC] network, recover their costs [of providing payphone service] from Carrier Common Line ("CCL") charges assessed on those carriers that connect with the incumbent LEC."<sup>6</sup>

This information is critical in developing a clear understanding of the controversial issues in these cases. It provides insight about the concern (i.e.: that LECs are subsidizing their payphone business through CCL charges), which the FCC is attempting to address when it talks about removing subsidies. Throughout the remainder of Section B of its Payphone Reclassification Orders, the FCC essentially defines and refines a three-step process for ensuring that the LECs' payphone service is essentially brought into parity with the independent payphone service providers service, and is no longer subsidized through CCL or other similar charges.

The three-step process to remove subsidies.

The three steps are easily identified in the orders, by topic:

Step 1: Requires the classification of LEC payphones as CPE and the unbundling of payphone "services" a LEC may be providing itself;

Step 2: Mandates transfer of payphone equipment to unregulated status;

Step 3: Provides for the termination of access charge compensation and other subsidies.

It is clearly anticipated by the FCC that, once a LEC accomplishes all three steps, it will be positioned to attest that it has satisfactorily complied with the intent of §276(b)(1)(B).

The first step is initially discussed in paragraph 142 of the Payphone Order. The FCC states that "to best effectuate the mandate of the Act . . ." the ILEC payphones (i.e. the payphone equipment) should be treated as unregulated, detariffed Customer Premises Equipment ("CPE"), to ensure that the costs associated with regulated services are separated from the competitive provision of the equipment used in conjunction with those services. In addition, the FCC explains, in paragraph 146, that because the ILECs use central office coin services but have not historically made them available to other PSPs, the FCC is also requiring the ILECs to unbundle and offer the individual central office coin services under non-discriminatory, public, tariffed offerings the ILEC provides to itself.

Paragraph 146 further states that, "Incumbent LECs not currently subject to price cap regulation, must submit cost support for their central office coin services, pursuant to Sections 61.38, 61.39, or 61.50(i) of the Commission's [FCC's] rules."<sup>7</sup> (emphasis added).

A very important distinction must be made at this point. Please note the specific language used by the FCC, as quoted from paragraph 146, above. Particular attention should be paid to the words "central office coin services". This language is important because, it is making reference to the very "services" the FCC is requiring the LECs to unbundle.

Despite the FCC's language and intent, most of the parties, at least in their initial briefs<sup>8</sup> in these causes, misread and/or misinterpreted that language to suggest that cost support would be required for "all" payphone services, including payphone access lines. That is simply not the case. The FCC clearly never intended for LECs to provide "cost support" for payphone access lines or prove that their access lines are cost-based. The Payphone Order only requires that the unbundled central office coin services and other

<sup>6</sup> Id. at para. 128.

<sup>7</sup> This would encompass all of the applicants named herein.

<sup>8</sup> 47 C.F.R. §§ 61.38, 61.39, or 61.50(i).

<sup>9</sup> See Briefs of the various parties filed on June 18, 1998, in the above-captioned causes.

similarly situated "services" be supported with cost-based data. It is for this reason, that the ILECs payphone access line rate is not required to be based upon unsubsidized cost based rates.

This interpretation is further supported by the FCC in its Reconsideration Order at paragraph 163, where the FCC draws a clear distinction between "LEC payphone services" and the actual payphone "lines" by stating, "LECs are not required to file tariffs for the basic payphone lines for smart and dumb payphones . . .". Such a statement would not make sense unless the FCC clearly intended to draw such a distinction between the unbundled "services" and the "lines".

This position is even further supported when one considers the impact of allowing a LEC, in a filing such as these, to implement a "cost-based" access line rate for a single "class" of customers—PSPs. It is difficult to imagine that the FCC would condone "piece-meal" ratemaking for a rate-of-return regulated entity. Nor, would it be logical for the FCC or this Commission to suggest "rate rebalancing" solely for payphone access lines, at the expense of the other classes of subscribers who receive the same type of access to the same type of line.

Despite the parties' previous suggestions to the contrary, it is inconsistent with the Payphone Reclassification Orders, and it would be irresponsible of Staff to condone the applicants' or this Commission's reliance on the cost support documentation the applicants' have provided thusfar, in support of increasing payphone access line rates. Such was not the intent of the FCC and it is certainly not in the public's interest.

The second step is discussed in the Payphone Order at paragraph 152. This step merely requires, at paragraph 159, that payphone assets be reclassified as non-regulated, either by maintaining the payphone assets on the carrier's books but treating the assets as non-regulated, or by transferring the payphone assets to a separate affiliate engaged in non-regulated activities. The FCC does further clarify that it does not consider "the loops connecting the payphones to the network, the central office "coin service", or operator service facilities supporting the ILECs' payphones" to be a payphone asset subject to reclassification.<sup>10</sup>

The final step specifically deals with the termination of access charge compensation and other subsidies. The FCC explains in paragraph 180, that "while independent payphone providers are required to pay the SLC for the loop used by each of their payphones . . .", LECs have not been required to pay this charge because the subscriber lines connected to LEC phones have historically been recovered entirely through the CCL charge.

It is for this reason that the FCC ordered incumbent LECs to reduce their interstate CCL charges by an amount equal to the interstate allocation of payphone costs currently recovered through those charges.<sup>11</sup> The end result of implementing this third and final step is that it effectively removes from regulated rate structures, all charges that previously recovered the costs of payphones.

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<sup>10</sup> See Id. at para. 159.

<sup>11</sup> See Id. at para. 181.

Conclusion.

Having provided a thorough review of the pertinent provisions of the statute and the Payphone Reclassification Orders, it should be apparent that the issue identified herein is not an issue. However, it is important that this Commission give consideration to where we have been and where we need to go with respect to these causes, and take this opportunity to get the parties back on track so we can see these causes to completion.

Respectfully submitted.

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## **Part II. Statutory Material**

safety, or property, from burglary, fire, vandalism, bodily injury, or other emergency, and

“(2) to transmit a signal regarding such threat by means of transmission facilities of a local exchange carrier or one of its affiliates to a remote monitoring center to alert a person at such center of the need to inform the customer or another person or police, fire, rescue, security, or public safety personnel of such threat, but does not include a service that uses a medical monitoring device attached to an individual for the automatic surveillance of an ongoing medical condition.

### **“SEC. 276. PROVISION OF PAYPHONE SERVICE.**

“(a) Nondiscrimination Safeguards.—After the effective date of the rules prescribed pursuant to subsection (b), any Bell operating company that provides payphone service—

“(1) shall not subsidize its payphone service directly or indirectly from its telephone exchange service operations or its exchange access operations; and

“(2) shall not prefer or discriminate in favor of its payphone service.

“(b) Regulations.—

“(1) Contents of regulations.—In order to promote competition among payphone service providers and promote the widespread deployment of payphone services to the benefit of the general public, within 9 months after the date of enactment of the Telecommunications Act of 1996, the Commission shall take all actions necessary (including any reconsideration) to prescribe regulations that—

“(A) establish a per call compensation plan to ensure that all payphone service providers are fairly compensated for each and every completed intrastate and interstate call using their payphone, except that emergency calls and telecommunications relay service calls for hearing disabled individuals shall not be subject to such compensation;

“(B) discontinue the intrastate and interstate carrier access charge payphone service elements and payments in effect on such date of enactment, and all intrastate and interstate payphone subsidies from basic exchange and exchange access



## **Title I—Telecommunication Services**

revenues, in favor of a compensation plan as specified in subparagraph (A);

“(C) prescribe a set of nonstructural safeguards for Bell operating company payphone service to implement the provisions of paragraphs (1) and (2) of subsection (a), which safeguards shall, at a minimum, include the nonstructural safeguards equal to those adopted in the Computer Inquiry-III (CC Docket No. 90-623) proceeding;

“(D) provide for Bell operating company payphone service providers to have the same right that independent payphone providers have to negotiate with the location provider on the location provider’s selecting and contracting with, and, subject to the terms of any agreement with the location provider, to select and contract with, the carriers that carry interLATA calls from their payphones, unless the Commission determines in the rulemaking pursuant to this section that it is not in the public interest; and

“(E) provide for all payphone service providers to have the right to negotiate with the location provider on the location provider’s selecting and contracting with, and, subject to the terms of any agreement with the location provider, to select and contract with, the carriers that carry intraLATA calls from their payphones.

“(2) Public interest telephones.—In the rulemaking conducted pursuant to paragraph (1), the Commission shall determine whether public interest payphones, which are provided in the interest of public health, safety, and welfare, in locations where there would otherwise not be a payphone, should be maintained, and if so, ensure that such public interest payphones are supported fairly and equitably.

“(3) Existing contracts.—Nothing in this section shall affect any existing contracts between location providers and payphone service providers or interLATA or intraLATA carriers that are in force and effect as of the date of enactment of the Telecommunications Act of 1996.

“(c) State Preemption.—To the extent that any State requirements are inconsistent with the Commission’s regulations, the Commission’s regulations on such matters shall preempt such State requirements.

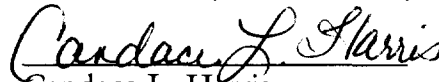
**APPENDIX B**  
**TO**  
**JOINT COMMENTS OF**  
**AMERICAN PUBLIC COMMUNICATIONS COUNCIL**  
**AND**  
**OKLAHOMA PAYPHONE ASSOCIATION**  
**(in CC Docket No. 96-128 and File No. CCB/CPD No. 99-31)**

**Analysis of Historic Costs for Payphone****Exhibit "A"**

	<b>Loop Costs</b>	<b>Switching Costs</b>	<b>Total Costs</b>
<b>Eaglenet, Inc.</b>	<b>31.68</b>	<b>19.62</b>	<b>51.30</b>
<b>Valliant Telephone Company</b>	<b>25.16</b>	<b>20.73</b>	<b>45.89</b>
<b>KanOkla Telephone Association, Inc</b>	<b>42.97</b>	<b>23.53</b>	<b>66.50</b>
<b>Santa Rosa Telephone Cooperative,</b>	<b>45.98</b>	<b>24.24</b>	<b>70.22</b>
<b>Oklahoma Telephone &amp; Telegraph</b>	<b>52.56</b>	<b>29.17</b>	<b>81.73</b>
<b>Chickasaw Telephone Company</b>	<b>41.41</b>	<b>19.86</b>	<b>61.27</b>
<b>Pine Telephone Company</b>	<b>32.08</b>	<b>32.56</b>	<b>64.64</b>

## CERTIFICATE OF SERVICE

I, Candace L. Harris, of Dickstein Shapiro Morin & Oshinsky, LLP, 2101 L Street, N. W., Washington, DC 20037, hereby certify that a copy of the foregoing Joint Comments of American Public Communications Council and the Oklahoma Payphone Association was served on this 4<sup>th</sup> day of November 1999, by hand delivery to the following parties:

  
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